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DEC 28 1949

CHARLES ELMORE CROPLEY

Supreme Court of the United States

OCTOBER TERM, 1949.

No. 505

TRANSPORT, TRADING & TERMINAL CORPORATION,

Petitioner,

against

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI.

ARTHUR A. BALLANTINE,
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1. The writ of certiorari should be issued in order that this Court may determine fundamental questions respecting the review of Tax Court decisions, viz.:

   (a) Whether the 1948 amendment of §1141(a) IRC, abrogating the rule of the *Dobson* case, empowered the Court of Appeals to try the case *de novo* on the record, reject the Tax Court's findings of fact and substitute contrary findings of its own; and

   (b) Whether the Court of Appeals could properly reverse the Tax Court, without a remand of the case for further hearing, upon an issue not presented to the Tax Court, viz.: whether the distribution of the Pacific-Atlantic stock should be disregarded on the theory that it did not constitute a "dividend" within the meaning of §115 (a) IRC 14

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2. The writ of certiorari should be issued to determine whether, as the Court of Appeals held, the rule of the *Gregory* case warrants the disregard of a valid and genuine corporate distribution on the theory that it was made for tax-saving purposes and was therefore not a "dividend" within the meaning of §115(a) IRC..... 20

3. The decision should be reviewed because the action of the court below in disregarding the distribution made by the petitioner conflicts in principle with this Court's decision in *General Utilities & Operating Co.* v. *Helvering*..... 22

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COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI.

To the Honorable, the Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

Summary Statement of the Matter Involved.

Petitioner prays that a writ of certiorari be issued to the United States Court of Appeals for the Second Circuit to review a judgment of that court rendered in the above case on October 4, 1949 (R. 71-72), reversing a decision of the Tax Court of the United States that the petitioner had overpaid its Federal income taxes for the calendar year 1940 in the amount of $167,767.62 (R. 14-15).

Petitioner submits that the Court of Appeals committed far-reaching errors of law which, if not corrected by this Court, will affect thousands of transactions and produce a mass of tax litigation.

The case arises out of a sale of certain stock by American-Hawaiian Steamship Company, parent of petitioner, under the following circumstances. On October 25, 1940, petitioner distributed, as a dividend in kind, to American-Hawaiian, its parent, 10,000 shares of stock of Pacific-Atlantic Steamship Company. On November 11, 1940, American-Hawaiian agreed to sell such shares for a net amount of $582,285. There were no negotiations for the sale of the stock prior to November 11, 1940, as the Tax Court found (R. 13). American-Hawaiian executed a contract for the sale of the stock on November 22, 1940 (R. 10).

American-Hawaiian, in its income tax return for 1940, reported the receipt of said shares as a dividend of the value of $582,285 (§115(j) IRC). The tax to American-Hawaiian on this amount, as an inter-company dividend subject to the dividends-received credit (§26(b) IRC), was $20,962.26. In accordance with established rules, American-Hawaiian treated the value of the dividend as its basis for the Pacific-Atlantic stock, and consequently reported no gain on the sale of that stock. (R. 9-11).

In reviewing petitioner's return for 1940, the Commissioner included in petitioner's income $562,285, which was the difference between the net proceeds of the sale by American-Hawaiian of the Pacific-Atlantic stock and the cost of that stock to petitioner, $20,000 (R. 11).

The Tax Court held that the foregoing transactions did not result in taxable gain to the petitioner. Specifically, the Tax Court found (R. 13) that negotiations for the sale of the Pacific-Atlantic stock by American-Hawaiian had not

> "even been started by the [petitioner] corporation prior to the distribution or dividend so as to bring the instant case within the rationale of * * * *Commissioner* v. *Court Holding Co.* [324 U. S. 331] * * *"

that the declaration of the dividend on October 21, 1940 was "genuine" and the transfer of the stock on October 25, 1940 was "unconditional and final" (R. 12), and that the "first intimation" that the purchaser would be willing to buy the stock was received on November 11, 1940, by American-Hawaiian (R. 13).

The Court of Appeals (hereinafter sometimes referred to as the "court below"), reversing the Tax Court, held that the distribution of the Pacific-Atlantic shares by petitioner to its parent should be disregarded and petitioner treated as retaining ownership of such shares until November 25, 1940, when they were sold by its parent.

The theory upon which the court below disregarded the distribution by petitioner to its parent was that such distribution was not "the kind of 'distribution'" contemplated by §115(a) of the Code,* defining dividends, because, according to the court below,

> "It was not a distribution for the purposes of the Parent's business, but only in order to escape a tax * * *."

The court below said that this theory represented an application of the doctrine of *Gregory* v. *Helvering*, 293 U. S. 465 (1935), which the court held to be controlling.

In arriving at its decision, the court below virtually tried the case *de novo* on the record before it. Its action in this respect raises important questions, requiring consideration by this Court, as to the scope of the powers of courts of appeals in reviewing decisions of the Tax Court.

(1) The court below found as a fact, without any support in the record and directly contrary to findings of the Tax Court fully supported by the record, that the ultimate purchaser of the Pacific-Atlantic shares had agreed with

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* Cited erroneously throughout the court's opinion as Section 115(2). The Code contains no Section 115(2).

petitioner that he would buy the shares at petitioner's election. The court below characterized this alleged arrangement as an "option" granted by the ultimate purchaser to petitioner (R. 41).*

(2) The court below found as a fact, although the Tax Court had made no finding one way or the other, that the distribution of the Pacific-Atlantic shares was made in order to save the tax which petitioner would have incurred if it had exercised the alleged so-called "option" to sell the shares (R. 41).

(3) Although the Commissioner, both in the Tax Court (R. 11) and before the court below (Brief, p. 15), had expressly disclaimed any contention that petitioner's separate entity should be disregarded, the court below found as a fact that petitioner was the "puppet" of its parent (R. 41), that it "had no independent will of its own" (R. 40), that the parent had "declared the dividend [of the Pacific-Atlantic shares] to itself" (R. 40), and that whether petitioner or its parent sold the shares was immaterial because "the proceeds of the sale were in any event to reach the same treasury" (R. 41).

The action of the court below in trying the case *de novo* constituted a clear departure from principles of appellate procedure established by this Court with respect to the review of Tax Court decisions.

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* The present case is clearly distinguishable from *Cumberland Public Service Co.* v. *United States*, 83 F. Supp. 843 (Ct. Cls. 1949), *cert. granted* October 17, 1949. In the *Cumberland* case a formal contract was entered into between the purchaser and the stockholders of the corporation for the sale of certain property, then owned by the corporation, which was later distributed to the stockholders and transferred by them. Here, however, petitioner did not agree to sell, nor did it offer to sell, the Pacific-Atlantic shares at any time, and its parent made no agreement or offer to sell at any time while petitioner owned the stock.

It is submitted that the court below also committed gross errors of substantive law which require correction by this Court:

(1) The validity and finality of a distribution by a corporation to its stockholders in no way depends upon whether the distribution is a dividend within §115(a) I. R. C. Until the court below rendered its opinion, no one had even suggested that §115(a) had anything to do with the case. Plainly, the section has no relation to the tax liabilities of a corporation *making* a distribution.

(2) Since the petitioner's liability in no way depended upon the application of §115(a) to the distribution, the sole ground upon which the court below sought to invoke the doctrine of the *Gregory* case disappears. The *Gregory* case held that a transaction which had been undertaken not for the purpose of reorganizing a business but of effecting the distribution of a parcel of shares was not an *exempt* transaction under the reorganization sections because not within the intendment of those sections.

The effort of the court below to assimilate the present case to the *Gregory* case by treating the petitioner *as if* it were relying upon §115(a)—a section having no application to the case—and then holding that this case is not within the "purpose" of that section is, we submit, a thin disguise for the *actual holding* of the court, viz., *that any transaction, no matter how genuine and final for all other purposes, is to be disregarded for tax purposes if undertaken with a tax-saving motive.* This startling doctrine was expressly rejected by this Court in the *Gregory* case and finds no support in any other decision of this Court.

(3) The decision of the court below conflicts in principle with this Court's decision in *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200 (1935), holding that a dis-

tribution of appreciated property in the form of readily marketable securities, which the stockholders were expected to sell, did not result in the realization of gain by the distributing corporation.

Petition for rehearing, filed July 26, was denied by the Court of Appeals, without opinion, on October 4, 1949.

Jurisdiction.

The jurisdiction of this Court is invoked under Section 1254(1) of the Judicial Code (28 U. S. C. §1254(1)) and Section 1141(a) of the Internal Revenue Code (26 U. S. C. §1141(a)).

The Opinions of the Courts Below.

The opinion of the Tax Court (R. 3-14) is reported in 9 T. C. 247. The opinion of the Court of Appeals for the Second Circuit (R. 37-41) is reported in 176 F. 2d 570.

Statutes Involved.

INTERNAL REVENUE CODE:

Sec. 22. GROSS INCOME. * * *

(e) *Distributions by Corporations.*—Distributions by corporations shall be taxable to the shareholders as provided in Section 115.

(f) *Determination of Gain or Loss.*—In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in Section 111.

Sec. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) *Computation of Gain or Loss.*—The gain from the sale or other disposition of property shall be the excess of

the amount realized therefrom over the adjusted basis provided in Section 113(b) for determining gain, • • •.

(b) *Amount Realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

Sec. 115. DISTRIBUTIONS BY CORPORATIONS.

(a) *Definition of Dividend.*—The term "dividend" when used in this chapter • • • means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year • • •.

(j) *Valuation of Dividend.*—If the whole or any part of a dividend is paid to a shareholder in any medium other than money the property received other than money shall be included in gross income at its fair market value at the time as of which it becomes income to the shareholder.

Sec. 1141. COURTS OF REVIEW.

(a) Jurisdiction.—

The courts of appeals shall have exclusive jurisdiction to review the decisions of the Tax Court • • • *in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury**; and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari in the manner provided in Section 1254 of Title 28 of the United States Code. • • •

(c) Powers.—

(1) TO AFFIRM, MODIFY, OR REVERSE.—Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require.

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* Italics denote amendment made by Public Law 773, §36 (80th Cong. 2nd Sess.).

Facts.

Transport, Trading & Terminal Corporation, the petitioner, is a New York corporation organized in 1935 for the purpose of engaging in shipping, terminal, dock and warehouse operations. It is, and always has been, a wholly-owned subsidiary of American-Hawaiian Steamship Company, a New Jersey corporation. In December, 1937, petitioner purchased 10,000 shares of stock of Pacific-Atlantic Steamship Company at a cost of $20,000. These shares represented an interest of approximately 20% in the common stock of Pacific-Atlantic. (R. 4-5.)

In June, 1940, the British Ministry of Shipping offered to purchase four ships from Pacific-Atlantic at $50.00 per deadweight ton. On June 10, 1940, C. E. Dant, who controlled about 40% of the stock of Pacific-Atlantic, called a meeting of some of the Pacific-Atlantic stockholders to discuss the offer of the British Ministry. Representatives of petitioner attended that meeting. Some of the stockholders of Pacific-Atlantic felt that the offer should be accepted. Dant was averse to accepting the offer. He stated to those present that if they did not insist on the sale of the ships he

> "would guarantee against any loss if the ships were not sold either by buying them [the ships] or working out some other arrangement." (R. 6-7, 17.)

In reliance upon Dant's statement, the other stockholders of Pacific-Atlantic agreed that the British offer should be declined (R. 17).

On October 21, 1940, petitioner's directors adopted a resolution declaring a dividend of the 10,000 shares of Pacific-Atlantic stock. On October 25, petitioner's certificate for such shares was endorsed and delivered to American-Hawaiian. Petitioner's policy had been to pay

out in dividends "a very large proportion of its earnings of each year." (R. 9-10.)

A meeting was held in New York on October 31, 1940, attended by Dant's attorney, representatives of American-Hawaiian and other stockholders of Pacific-Atlantic. After discussion of Dant's assurance to the Pacific-Atlantic stockholders on June 10, 1940, Dant's attorney inquired whether the group present would agree to the sale of Pacific-Atlantic's *ships* to Dant or to one of his companies at $35 per ton. (The price which the British Ministry had offered in June was $50 per ton.) The other stockholders rejected this suggestion. (R. 10, 13.)

A later meeting was arranged at San Francisco on November 11, 1940. At that meeting Dant renewed the previous proposal of a sale of Pacific-Atlantic's *ships* to him at $35 per ton. "The rest of the stockholders would not agree" and "the meeting broke up without agreement" (R. 10). Later, the meeting was resumed and ultimately Dant stated that he or one of his companies would offer $60.00 per share for the Pacific-Atlantic *stock*,

> "if the stockholders would all go in on the undertaking and adjust the price in case of additional taxes being levied against Pacific-Atlantic but with no escrow or bond." (R. 10; Tr. 145.)

The Tax Court found that Dant's offer of November 11 *"was the first intimation to American-Hawaiian that Dant would be willing to buy the Pacific-Atlantic stock instead of the ships"** (R. 13).

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* This finding was based, in part, upon the testimony of Dant, a disinterested witness, that he made no offer to buy the outstanding Pacific-Atlantic stock (Tr. 52, 57); that he was "not in a position to make such an offer for several reasons" including his lack of knowledge as to certain liabilities of Pacific-Atlantic (R. 13, Tr. 52); and that the uncertainty as to what would be done to carry out his assurance of June 10 to the other stockholders continued "until November" (R. 7, 13, Tr. 55).

A final agreement for the sale was drafted and executed by American-Hawaiian and States Steamship Company, a Dant company, on November 22, 1940. Pursuant to such agreement, the sales price of $60 per share was later adjusted to $58.22 per share—approximately $5 per share less than the book value of $63.11 per share determined by Dant's accountants. (R. 8-10.)

Decisions Below.

The Tax Court held that petitioner was not to be taxed as having realized a gain because it merely parted with property, receiving nothing in return, and neither struck a bargain, nor negotiated with the ultimate purchaser, for a sale of the property distributed. The Tax Court held (R. 12-13) that the sale of the Pacific-Atlantic shares by American-Hawaiian in November, 1940 was not, in substance, a sale by petitioner, under the rule of *Commissioner* v. *Court Holding Co., supra,* 324 U. S. 331 (1945), because negotiations for the sale of the shares had not "even been started" prior to the distribution.

The Tax Court further held that *Gregory* v. *Helvering, supra,* 293 U. S. 465 (1935), did not warrant disregard of the distribution to the parent and the taxation of gain to the petitioner, stating (R. 12, 14):

> "Generally, individuals organize business corporations with the expectation that dividend payments will eventually result from their operations. It is the province of the corporate directors to determine the time and the character of the dividend payment. It is unimportant here whether the stockholder is an individual or a corporate entity. If the declaration of a dividend is genuine and the transfer is unconditional and final it is effective as such. *Only where the transaction is unreal or a sham may it be disre-*

> *garded for tax purposes. The respondent makes no such claim here."*
>
> • • • • • •
>
> "In the circumstances, the conceded fact that when the dividend in kind was declared petitioner had knowledge that if Pacific-Atlantic were liquidated or its shares purchased it would have a large taxable gain is of no legal significance. *Gregory* v. *Helvering* [293 U. S. 465] • • •." (Italics added.)

The Tax Court also rejected, as contrary to this Court's decision in *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200 (1935), the Commissioner's contention that, apart from the subsequent sale, the appreciation in value of the Pacific-Atlantic shares was realized by the petitioner merely by the distribution of such shares to its parent as a dividend in kind.

Although the record fully supported the Tax Court's finding that the first intimation that Dant would be willing to buy the Pacific-Atlantic stock came on November 11, 1940, after petitioner had parted with the stock, the court below made a contrary finding of its own (R. 40)—that Dant had granted the stockholders of Pacific-Atlantic, petitioner included,

> "an option to sell the shares to him, if they elected to do so."

This finding was based on the court's *assumption* that Dant's obligation to buy the *ships*, or produce a buyer therefor, at $50 per ton was the legal and practical equivalent of an agreement on Dant's part that, at petitioner's election, he would buy the Pacific-Atlantic stock "at $50 a ton" (R. 40).

The court's assumption is without warrant. First, it overlooks the fact that the value of the Pacific-Atlantic

shares depended not only upon the value of the ships but, among other things, upon the amount of Pacific-Atlantic's liabilities, disclosed and undisclosed, including undetermined tax liabilties. Dant testified that because he had no knowledge as to these undisclosed liabilities he was in no position to make an offer for the stock (Tr. 52, 53). Secondly, if Dant had merely purchased the ships, which was all that he was obliged to do, petitioner and the other stockholders of Pacific-Atlantic would have been left with their investment in the company, on which they could realize only by finding a purchaser or through liquidation of the company. Petitioner, as the holder of only 20% of the stock, would have been in no position to compel the liquidation of the company. Had Dant, after purchasing the ships, then decided to put the company into other shipping ventures, rather than liquidate it, petitioner could not have prevented such action.

The court below having found, however, that Dant, by agreeing to buy certain *ships* of Pacific-Atlantic, had agreed to buy the *stock* of Pacific-Atlantic at petitioner's "option" (R. 40), proceeded to hold that the declaration and payment of the dividend of Pacific-Atlantic stock should be disregarded, and the subsequent sale imputed to petitioner, on the theory that the distribution was made for tax-saving reasons and was therefore (R. 40):

> "not the kind of 'distribution' which the statute [§115(a)] had in mind; it was not a 'dividend' declared in the ordinary course of business."

The court went on to say (R. 41):

> "* * * we hold that the 'long-term capital gain'—§117(a) (4)—*was realized by the taxpayer on November 25, because* under the decisions we have already cited, *the declaration of the dividend* on

October 21 *was not that kind of 'distribution' which §115(a) presupposes* * * *." (Italics added.)

This novel theory was developed by the court below in an effort to assimilate the case to *Gregory* v. *Helvering, supra* (293 U. S. 465).

Questions Presented.

1. Did the Court of Appeals err as a matter of law (a) in substituting its own findings of fact for contrary findings of fact of the Tax Court, and (b) in reversing the Tax Court, without a remand for further hearing, upon an issue not presented to the Tax Court, viz.: whether the distribution of the Pacific-Atlantic stock should be disregarded on the theory that it was not a "dividend" within the provisions of §115(a) IRC?

2. Did the Court of Appeals err in holding that the question whether the distribution made by petitioner was a "dividend" within the meaning of §115(a) was determinative of the question whether petitioner subsequently realized taxable gain upon the sale by American-Hawaiian of the property distributed?

3. Did the Court of Appeals err in holding that the doctrine approved by this Court in *Gregory* v. *Helvering*, 293 U. S. 465 (1935), warrants the disregard of a genuine, valid and complete distribution of property to a corporation's stockholder if motivated by tax considerations?

4. Does the decision of the Court of Appeals as to the tax consequences of a distribution in kind under the facts of this case conflict in principle with this Court's decision in *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200 (1935)?

Reasons Relied on for Allowance of the Writ.

1. The writ of certiorari should be issued in order that this Court may determine fundamental questions respecting the review of Tax Court decisions, viz.:

(a) Whether the 1948 amendment of §1141(a) IRC, abrogating the rule of the *Dobson* case, empowered the Court of Appeals to try the case *de novo* on the record, reject the Tax Court's findings of fact and substitute contrary findings of its own; and

(b) Whether the Court of Appeals could properly reverse the Tax Court, without a remand of the case for further hearing, upon an issue not presented to the Tax Court, viz.: whether the distribution of the Pacific-Atlantic stock should be disregarded on the theory that it did not constitute a "dividend" within the meaning of §115(a) IRC.

(a) The decision of the Court below was based upon its finding that petitioner had obtained an agreement from Dant which obligated him to buy the Pacific-Atlantic shares at petitioner's election. In making such finding—which is squarely contrary to the Tax Court's findings (R. 13)—the Court of Appeals departed from principles of appellate procedure established by decisions of this Court and which were stated in *Wilmington Trust Co.* v. *Helvering,* 316 U. S. 164 (1942), as follows (p. 168):

> "It is the function of the Board, not the Circuit Court of Appeals, to weigh the evidence, *to draw inferences from the facts, and to choose between conflicting inferences.* The court may not substitute its view of the facts for that of the Board. *Where the findings of the Board are supported by substantial evidence they are conclusive.* * * * Under the statute, the court may modify or reverse the decision of the Board only if it is 'not in accordance with law.' 44 Stat. 110, 26 U. S. C. §1141(c)(1)." (Italics added.)

In *Helvering* v. *National Grocery Co.*, 304 U. S. 282 (1938), this Court said (p. 294):

> "The Court of Appeals, instead of limiting its review to ascertaining *whether there was evidence to support the Board's findings and decision,* made on all the evidence, as upon a trial *de novo,* in effect an independent determination of the matters which had been in issue before the Board. The court was without power to do so." (Italics added.)

These cases, and numerous others to the same effect,* were based upon the following statutory provision, now contained in §1141(c)(1) IRC, limiting the *powers* of appellate courts with respect to the review of Tax Court decisions:

> "(1) To AFFIRM, MODIFY, OR REVERSE.—Upon such review such courts shall have power to affirm or, *if the decision of the Board is not in accordance with law,* to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require." (Italics added.)

In 1948, Congress (by Public Law 773, §36, 80th Cong., 2d Sess.) amended §1141(a), *supra,* providing that courts of appeals have exclusive *jurisdiction* to review Tax Court decisions, by adding the phrase:

> "in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury".

No change was made in the provisions of §1141(c)(1), quoted above.

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* The cases are listed in footnote 22 in this Court's opinion in *Dobson* v. *Commissioner,* 320 U. S. 489 (1943).

The court below apparently considered that, as a result of the amendment to §1141(a), it was authorized under Rule 52(a) of the Rules of Civil Procedure* to substitute findings of fact of its own for findings of the Tax Court which it conceived to be "clearly erroneous."

The conflict between the action taken by the court below and the decisions of this Court under §1141(c)(1) was called to the attention of the court below in a petition for rehearing, which was denied without opinion. In effect, therefore, the court below has held that, upon review of Tax Court decisions, courts of appeals are no longer confined to ascertaining whether "there was evidence to support the Board's findings and decision" but are free to try the case *de novo*.

It is respectfully submitted that this question should be passed upon by this Court.

The purpose of the 1948 amendment of §1141(a) was to abrogate the rule of *Dobson* v. *Commissioner*, 320 U. S. 489 (1943) (see Senate Report No. 1559, 80th Cong., 2d Sess., pp. 2, 13). In the *Dobson* case this Court held (p. 502) that appellate courts were empowered to reverse the Tax Court only in a case where the court could "separate the elements of a decision so as to identify a clear-cut mistake of law." Since the *Dobson* case narrowed very considerably the latitude which had previously been allowed to reviewing courts, it follows that Congress, in abrogating the rule of the *Dobson* case, did not necessarily intend to nullify the effect of §1141(c)(1) as interpreted in the *National Grocery, Wilmington Trust* and like decisions rendered prior to the decision in the *Dobson* case.

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* Rule 52(a) provides in part:

> "Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses."

The intent of Congress not to abrogate §1141(c)(1) appears affirmatively from the legislative history of Public Law 773 (which amended §1141(a)). This history shows that the original bill (H. R. 3214, 80th Cong.) proposed the repeal of §1141 in its entirety, whereas the bill, as finally enacted, made no change in §1141(c)(1), defining the *powers* of reviewing courts, but merely broadened the *jurisdiction* of courts of review by making the above-quoted amendment to §1141(a). See H. R. 3214, §§271, 1294, and Schedule of Laws Repealed, p. 786, as it passed the House.

Even if §1141(c)(1) no longer prevents a substitution by a court of appeals of its own findings of fact for those of the Tax Court, Rule 52(a) would not authorize such procedure in the present case. This is made clear by the recent decision of this Court in *United States* v. *Yellow Cab Company*, October Term, 1949, No. 22 (Dec. 5, 1949). There the Government asked this Court to retry issues of fact in an antitrust suit which were in many respects similar to the issues of fact which the Court of Appeals proceeded to retry in this case. In refusing to do so, this Court said:

> "It ought to be unnecessary to say that Rule 52 applies to appeals by the Government as well as to those by other litigants. There is no exception which permits it, even in an antitrust case, to come to this Court *for what virtually amounts to a trial de novo on the record of such findings as intent, motive and design.* While, of course, it would be our duty to correct clear error, even in findings of fact, the Government has failed to establish any greater grievance here than it might have *in any case where the evidence would support a conclusion either way* but where the trial court has decided it to weigh more heavily for the defendants. *Such a choice between two permissible views of the weight of evidence is not 'clearly erroneous'.*" (Italics added.)

A fortiori, in the present case, the findings of the Tax Court cannot properly be held to be "clearly erroneous" where there was no evidence contrary to the finding that Dant made no agreement with the petitioner to purchase the Pacific-Atlantic stock, and where the Government itself did not attack the correctness of such finding before the court below, either by way of assignment of error or otherwise.

Petitioner submits that under these circumstances the court below was without power, either under §1141(c)(1) IRC or Rule 52(a) of the Rules of Civil Procedure, to make its own independent findings of fact as to the scope of Dant's undertaking and thereby substitute its view of the facts for that of the Tax Court.

(b) The court below could not properly reverse, without a remand, upon an issue not presented to the Tax Court.

The court below held (R. 41) that the gain

> "• • • was realized by the taxpayer on November 25, because under the decisions we have already cited, the declaration of the dividend on October 21 was not that kind of 'distribution' which §115(a) presupposes."

In order to arrive at this conclusion the court below found it necessary to disregard the separate entities of petitioner and its parent. It did so by finding that "the Parent's will was the taxpayer's, which had no independent will of its own", that "Parent, acting through the taxpayer, • • • declared the dividend to itself", that the petitioner was "the Parent's puppet", and that since the proceeds of any sale of the Pacific-Atlantic stock "were in any event to reach the same treasury" it was "altogether irrelevant that the title to the shares passed from the Parent or not from the taxpayer" (R. 40-41).

Petitioner was not required to meet any such issue before the Tax Court because the Commissioner disclaimed any contention that the separate entities of petitioner and its parent should be disregarded. The Tax Court opinion expressly states that the Commissioner made no such contention (R. 11). Before the Court of Appeals, the Commissioner again disclaimed any such contention (Brief, p. 15).

Therefore, even if the court below was correct in holding that the petitioner's liability depended upon whether the distribution of the Pacific-Atlantic stock was a "dividend" within the meaning of §115(a), the court below was not authorized to reverse on this ground and sustain the deficiency. *General Utilities & Operating Co.* v. *Helvering,* 296 U. S. 200 (1935). The court, having determined to reverse on such issue, should have remanded the case for a further hearing thereon, pursuant to the provisions of §1141(c)(1) IRC authorizing courts of appeal, when reversing for errors of law, to remand the case "for rehearing, as justice may require". *Hormel* v. *Helvering,* 312 U. S. 552 (1941).

In the *Hormel* case the question was raised for the first time before the circuit court whether the taxpayer, as grantor of a trust, was taxable on the income thereof under the provisions of §22(a). The circuit court reversed the Tax Court and held the grantor taxable on that theory. This Court agreed with the circuit court, but held that the case should have been remanded, saying (p. 560):

> "But the Board of Tax Appeals neither found the facts nor considered the applicability of 22(a) in the light of the *Clifford* case. Congress has entrusted the Board with exclusive authority to determine disputed facts. Under these circumstances we do not feel that petitioner should be foreclosed

from all opportunity to offer evidence before the Board on this issue, however remote may be his chance to take his case out of the *Clifford* rule. Accordingly, the judgment of the lower court reversing the decision of the Board of Tax Appeals is affirmed, with directions to the Board of Tax Appeals for further proceedings in accordance with this opinion."

2. The writ of certiorari should be issued to determine whether, as the Court of Appeals held, the rule of the *Gregory* case warrants the disregard of a valid and genuine corporate distribution on the theory that it was made for tax-saving purposes and was therefore not a "dividend" within the meaning of §115(a) IRC.

It is submitted that this holding of the Court of Appeals, if correct, involves a new and important principle of federal income tax law which has not been, but should be, passed upon by this Court.

The *Gregory* case, *supra* (293 U. S. 465) did not hold that the tax consequences of transactions depend on whether they have a "business purpose" or a tax-saving purpose.

The facts of the *Gregory* case were that the taxpayer owned all the shares of United Mortgage Corporation, which owned 1,000 shares of Monitor Securities Co. The taxpayer desired to sell the Monitor shares. She caused the organization of the Averill Corporation and the transfer to Averill of the Monitor shares in exchange for the issuance of the Averill shares to her. Three days later, Averill was dissolved and the taxpayer received the Monitor shares as a liquidating distribution and sold them.

The taxpayer, Gregory, claimed that the transfer from United to Averill was "a transfer by a corporation of * * * a part of its assets to another corporation" of which taxpayer, the transferor's stockholder, was in control imme-

diately thereafter, and that therefore the transactions were within one of the statutory definitions of a "reorganization" and, as such, were exempt from tax.

This Court held that the transactions did not come within the statutory exemption because they represented, not a plan "to reorganize a business or any part of a business, but to transfer a parcel of corporate shares to the petitioner" (293 U. S. at p. 469).

This Court deemed the tax-saving motive in the transaction to be wholly irrelevant, saying (pp. 469-470):

> "the question for determination is whether what was done, apart from the tax motive, was the thing which the statute intended.
>
> • • • • • •
>
> The rule which excludes from consideration the motive of tax avoidance is not pertinent to the situation, because the transaction upon its face lies outside the plain intent of the statute."

Here, therefore, the petitioner's motive in distributing the Pacific-Atlantic stock was not only not controlling but was altogether immaterial. No question could arise under the rule of the *Gregory* case because the petitioner did not rely upon the reorganization provisions or any other *statutory provision* to relieve it of tax liability. Petitioner simply relied upon the *fact* that it had distributed the stock to its parent and that the parent had made the sale of the stock.

Since the Tax Court had found that the distribution *was a fact* and that the sale *was made* by the parent, the Court of Appeals, in order to frustrate a tax-saving which it deemed objectionable, was obliged, *first*, to treat the petitioner *as if* it had relied upon a statute to relieve it of tax liability and, *second*, to hold that the transaction was not within the purpose of the imputed statute and was therefore not exempt thereunder.

The statute which the court seized upon, in its effort to assimilate the case to the *Gregory* case, was §115(a), defining a "dividend" as "any distribution made by a corporation to its shareholders, whether in money or in other property" out of the earnings and profits of the distributing corporation.

But it is perfectly clear that the petitioner's tax liability does not depend on whether the distribution of the Pacific-Atlantic stock was a "dividend" within the meaning of §115(a). What controls is not a statute governing the tax treatment of distributions *received* by stockholders but the *fact* that the distribution of the Pacific-Atlantic stock was made by the petitioner and that petitioner received nothing in return therefor. The court's holding that the distribution here should be disregarded is nothing more or less than a holding that the tax consequences of a transaction depend not upon what was done but upon the presence or absence of a tax-saving motive.

Under the novel theory adopted by the court below, if an owner of real estate, following a common practice in late years, tore down a house to avoid liability for real estate taxes from year to year, he would still have to pay taxes on the house, the tearing down being disregarded as a scheme to avoid tax liability.

It is submitted that it is important to taxpayers generally, to the Commissioner and to the lower courts to learn from this Court whether the decision of the court below represents a correct application of the *Gregory* case.

3. The decision should be reviewed because the action of the court below in disregarding the distribution made by the petitioner conflicts in principle with this Court's decision in *General Utilities & Operating Co.* v. *Helvering*.

Before the Tax Court, the Commissioner contended that the distribution of Pacific-Atlantic stock of itself con-

stituted a realization by petitioner of the excess of the appreciation in value of such stock over the cost thereof to petitioner, the distributing company. The Tax Court rejected this contention as contrary to the decision of this Court in *General Utilities & Operating Co.* v. *Helvering, supra* (296 U. S. 200) wherein this Court held that the distribution of appreciated property did not result in the realization of gain by the distributing corporation.

In recent years the question whether the distribution of appreciated property gives rise to gain by the distributing company has been almost constantly before the Tax Court. Thus, since 1944, the Tax Court has been called upon to review at least eleven cases*, in addition to the present case, in which the Commissioner determined that corporations realized gain upon the distribution of appreciated property. During the same period the Tax Court has reviewed twelve other cases** in which the Commissioner

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* *Beach Petroleum Corp., Ltd.*, memo. op. 5 T. C. M. 638 (1946); *Scientific Production Corp.* memo. op. 4 T. C. M. 328 (1945); *J. A. Folger & Co.*, memo. op. 4 T. C. M. 710 (1945); *Southwest Consolidated Corp.*, memo. op. 5 T. C. M. 6 (1946); *Marlen Realty Co.*, memo. op. 3 T. C. M. 1178 (1944), Comm'r's appeal dismissed, 151 F. 2d 1016 (8th Cir. 1945); *Earle Real Estate Co.*, memo. op. 6 T. C. M. 667 (1947); *J. L. Washburn Estate, Inc.*, memo. op. 3 T. C. M. 1192 (1944); *Nemours Corp.*, memo. op. 6 T. C. M. 820 (1947); *Columbia Development Corp.*, memo. op. 6 T. C. M. 548 (1947); *Horne Oil Co.*, memo. op. 6 T. C. M. 233 (1947); *Smith Bros. Refinery Co., Inc*, memo. op. 5 T. C. M. 17 (1946).

** *Jane E. Bradley*, 9 T. C. 115 (1947); *Paulina D. Dean*, 9 T. C. 256 (1947); *Herbert G. Hanan*, memo. op. 3 T. C. M. 670 (1944); *John H. Acheson, Est.* memo. op. 3 T. C. M. 1242 (1944); *Elizabeth N. Sager*, memo. op. 3 T. C. M. 1176 (1944); *Edith K. Timken*, memo. op. 3 T. C. M. 631 (1944); *Carl A. Fisher*, memo. op. 3 T. C. M. 393 (1944); Comm'r's appeal dismissed 150 F. 2d 1019 (10th Cir. 1945); *National Carbon Co.*, 2 T. C. 57 (1943); *Walter B. Congdon*, memo. op. 3 T. C. M. 516 (1944); *Charles R. McLean*, memo. op. 3 T. C. M. 1174 (1944); *Howard C. Platt Trust*, memo. op. 4 T. C. M. 715 (1945), Comm'r's appeal dismissed, 154 F. 2d 1016 (9th Cir. 1946); *G. W. Grandin*, memo. op. 4 T. C. M. 1031 (1945). See also *Comm'r* v. *Timken Estate*, 141 F. 2d 625 (6th Cir. 1944), aff'g 47 B. T. A. 494 (1942).

determined that such a distribution gave rise to "earnings and profits" so as to fix the character of the distribution as a taxable dividend. In each of such cases, the Tax Court overruled the Commissioner's determination.

If the decision of the Court below is permitted to stand, however, the Commissioner will have accomplished his purpose of upsetting the holding of the *General Utilities* case, at least in the great majority of cases where the distribution in kind is made in the expectation that the stockholders will sell the distributed property (which they are frequently obliged to do in order to find the funds with which to pay the tax on the dividend). In form, the tax will not be imposed on the theory that distribution of the appreciated property was a realization of gain. The same result will be accomplished, however, by the formula of (a) disregarding the distribution and (b) taxing the distributing corporation on the excess of the proceeds from the stockholder's sale over the basis which the property had in the hands of the corporation.

This result cannot be reconciled in principle with the holding of this Court in the *General Utilities* case, where readily marketable securities were distributed in the expectation that they would be sold. Neither can it be reconciled with the statutory provisions limiting taxable gain on the "sale or other disposition of property" to the excess of the money or property *received* over the basis of the property (§22(f) and §111 IRC).

It is submitted that the decision below calls for a restatement by this Court of the principle, established by the *General Utilities* case, that a corporation distributing appreciated property, which it has not agreed to sell, realizes no gain as a result of the distribution for the reason that it has merely parted with property, receiving nothing in return.

Conclusion.

The petition for a writ of certiorari should be granted in order

(1) to determine whether appellate courts have power to substitute their own findings of fact for findings made by the Tax Court which are based upon substantial evidence;

(2) to correct the gross procedural error committed by the court below in reversing the decision of the Tax Court, without a remand for further hearing, upon an issue which was not tried in the Tax Court, viz., whether the distribution by petitioner to its parent should be disregarded on the theory that it was not a "dividend" within the meaning of §115(a);

(3) to determine whether the court below correctly applied, or completely distorted, the principle of this Court's decision in the *Gregory* case by holding that any transaction entered into with a tax-saving motive may be disregarded in order to impose a tax; and

(4) to resolve the essential conflict between the decision of the court below, that a distribution in kind may be disregarded if made with expectation of sale, and the holding of this Court in the *General Utilities* case.

Respectfully submitted,

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